

**DEPARTMENT OF STATE REVENUE**  
**LETTER OF FINDINGS NUMBER: 01-0143**  
**State Gross Retail Tax—Burden of Proof for Exemptions**  
**Tax Administration—Penalty**  
**For Tax Year 1997**

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**ISSUES**

**I. State Gross Retail Tax—Burden of Proof for Exemptions**

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| <b><u>Authority:</u></b> | IC § 6-2.5-2-1 | 45 IAC 2.2-2-1  |
|                          | IC § 6-2.5-3-2 | 45 IAC 2.2-2-2  |
|                          | IC § 6-8.1-5-1 | 45 IAC 2.2-5-53 |
|                          |                | 45 IAC 2.2-8-2  |
|                          |                | 45 IAC 2.2-8-12 |

Taxpayer protests the state gross retail tax assessment on items for which taxpayer claims to have valid exemptions.

**II. Tax Administration—Penalty**

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| <b><u>Authority:</u></b> | IC § 6-8.1-10-2.1 | 45 IAC 15-11-2 |
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Taxpayer protests the assessment of the 10% negligence penalty.

**STATEMENT OF FACTS**

Taxpayer was a wholesale distributor of consumer electronics (satellite dishes). In addition, taxpayer sold C-Band programming through its programming operation, and a maintenance service department to repair various pieces of equipment sold to customers. Effective in January of 1998, taxpayer merged into another satellite dish corporation. Further facts will be added as necessaryI. State Gross Retail Tax—Burden of Proof for Exemptions

**DISCUSSION**

Taxpayer protests the assessment of state gross retail tax on items for which taxpayer claims to have sold subject to valid exemptions. The auditor reviewed sales invoices for satellite equipment sales for October 1997, stating that this month was closest to the average monthly sales for 1997. At the hearing, taxpayer took issue with the selection, arguing that October, part of taxpayer's fourth quarter sales, was highly inflated due to an increase in purchases of high-

ticket items in anticipation of the holidays. While there is a projection agreement form in the file, it was not signed by taxpayer's representative. The auditor indicates that the taxpayer's representative at the time of the audit was aware that the sales invoices for October 1997 would be used as the time frame for projecting taxpayer's 1997's gross retail tax liability. Taxpayer argued at the hearing that to use the company's most productive month as the basis for the projection was unjust. However, there is nothing in the statutes or regulations circumscribing an auditor's choice of time frames for projecting results.

Taxpayer's major argument is that the Department did not give taxpayer credit on all certificates and affidavits sent to the auditor as proof that taxpayer was selling satellite dishes to purchasers for resale. In as much as some of taxpayer's out-of-state customers, who are not registered to do business in Indiana, are within a short enough driving distance to a distribution center that they prefer driving for pick-up rather than paying shipping charges, a brief examination of the applicable statutes and regulations is in order.

Under IC § 6-8.1-5-1(b), a "notice of proposed assessment is *prima facie* evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made. IC § 6-2.5-2-1 imposes an "excise tax, known as the state gross retail tax . . . on retail transactions made in Indiana." Second, IC § 6-2.5-3-2 also imposes an excise tax, "known as the use tax," "on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction." *See also*, 45 IAC 2.2-2-1, 45 IAC 2.2-2-2, and 45 IAC 2.2-3-4, regulations defining terms in the statute imposing the state gross retail tax, and setting forth the retail merchant's duty to collect the tax.

The above statutes and regulations clearly state that tax is assessed and the retail merchant collects and remits the tax to the State of Indiana *unless* the retail merchant—taxpayer—supplies proof sufficient to either avoid the liability in the first instance, or defend against the liability during an audit.

45 IAC 2.2-8-2 states that "a retail merchant may not make a retail transaction in Indiana" without a retail merchant's certificate. Out-of-state merchants "*may* register with the Indiana Department of Revenue to collect and remit Indiana *use* tax on sales to Indiana purchasers." (Emphasis added). This regulation applies to use tax, not the state's gross retail tax, and applies to sales from outside Indiana to customers within Indiana. This regulation does not apply to out-of-state merchants buying products in Indiana to sell to their own customers in their own states.

For example: a Kentucky retail merchant orders satellite dishes from taxpayer, and taxpayer, instead of shipping the items, makes them available for pick-up at the Kentucky merchant's request. When an out of state customer comes into the state, they are no longer from out of state; they are no longer a retail merchant, but a customer. But for the Kentucky merchant's desire to avoid shipping charges, these types of sales would fall into the category of interstate commerce and would therefore be exempt pursuant to 45 IAC 2.2-8-12(e). However, when the taxpayer acquires physical possession and title to goods in Indiana, this is fully an Indiana transaction. Absent valid Indiana exemption certificates from these customers, taxpayer must establish that these sales were indeed exempt purchases.

## **FINDING**

Taxpayer's protest concerning state gross retail taxes assessed for sales where taxpayer's proof consists of affidavits and out-of-state exemption certificates is sustained to the extent the Audit Division can determine exempt transactions from the affidavits and information contained in out of state exemption certificates.

## **II. Tax Administration—Penalty**

### **DISCUSSION**

Taxpayer protests the imposition of the 10% negligence penalty. Taxpayer argues that its failure to pay the appropriate amount of tax due was based solely on taxpayer's interpretation of the relevant statutes, regulations, and case law.

Indiana Code Section 6-8.1-10-2.1(d) states that if a taxpayer subject to the negligence penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit tax held in trust, or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall waive the penalty. Indiana Administrative Code, Title 45, Rule 15, section 11-2 defines negligence as the failure to use reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence results from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by Indiana's tax statutes and administrative regulations.

In order for the Department to waive the negligence penalty, taxpayer must prove that its failure to pay the full amount of tax due was due to reasonable cause. Taxpayer may establish reasonable cause by "demonstrat[ing] that it exercised ordinary business care and prudence in carrying or failing to carry out a duty giving rise to the penalty imposed. . . ." In determining whether reasonable cause existed, the Department may consider the nature of the tax involved, previous judicial precedents, previous department instructions, and previous audits.

In this instance, taxpayer attempted to maintain records of out-of-state purchases, and to substantiate them during the audit procedure. Taxpayer had reasonable cause to believe it had fully complied with Indiana's gross retail tax statutes and regulations.

## **FINDING**

Taxpayer's protest concerning the abatement of the 10% negligence penalty is sustained.